

**BEFORE THE POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001**

Annual Compliance Report, 2014

Docket No. ACR2014

COMMENTS OF PITNEY BOWES INC.

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I. INTRODUCTION

Pitney Bowes Inc. (Pitney Bowes) respectfully submits these comments on the Annual Compliance Report for Fiscal Year 2014, filed by the Postal Service on December 29, 2014 (FY2014 ACR). These comments address: (1) the disparity in the cost coverage and unit contribution of First-Class Mail Single-Piece and Presort Letters / Cards, (2) First-Class and Standard Mail Automation Letters rate design, (3) the positive effect of the newly introduced rate differential between Metered Letters and Stamped Letters, and (4) First-Class Mail Flats costing issues.

II. DISCUSSION

A. FY2014 ACR Data Confirm a Continuing Disparity in the Cost Coverage and Unit Contribution of First-Class Single-Piece and Presort Letters

The FY2014 ACR confirms that First-Class Mail Presort Letters / Cards continue to be much more profitable than Single-Piece First-Class Mail Letters / Cards. In FY2014, the unit contribution for First-Class Mail Presort Letters / Cards was 26.0 cents, 5.2 cents greater than the 20.8 cent unit contribution of Single-Piece First-Class Mail Letters / Cards. *See* USPS-FY14-1. Public_FY14CRA, “Cost1.” The FY2014 ACR data also confirm a disparity in the cost coverage between Presort Letters / Cards and Single-Piece Letters / Cards. For FY2014 the cost coverage for Presort Letters / Cards is 320.2 percent, as compared to the cost coverage for Single-Piece Letters / Cards of 174.8 percent. *See id.*

As shown in Table 1 below, this disparity in unit contribution and cost coverage has existed since at least 2008 when the Postal Service began reporting costs and revenues by product.

| Table 1. Single-Piece Letters / Cards and Presort Letters / Cards Unit Contribution and Cost Coverage (FY2008-FY2014) ¹ | | | | |
|---|---|--|--|---|
| | Single-Piece Letters/Cards Unit Contribution | Presort Letters/Cards Unit Contribution | Single-Piece Letters/Cards Cost Coverage | Presort Letters/Cards Cost Coverage |
| FY 2014 | \$0.208 | \$0.260 | 174.8% | 320.2% |
| FY 2013 | \$0.191 | \$0.246 | 169.7% | 310.5% |
| FY 2012 | \$0.181 | \$0.233 | 165.9% | 292.0% |
| FY 2011 | \$0.170 | \$0.232 | 161.2% | 298.8% |
| FY 2010 | \$0.174 | \$0.229 | 164.0% | 295.9% |
| FY 2009 | \$0.171 | \$0.223 | 164.9% | 290.4% |
| FY 2008 | \$0.169 | \$0.218 | 167.1% | 298.1% |

The continuing disparity in unit contribution and cost coverage cannot be justified. It harms the Postal Service financially and discourages the growth and retention of the most profitable First-Class Mail products.

Under the CPI price cap, the overall amount of First-Class Mail revenue is limited, but the Postal Service can use its pricing authority to increase the contribution that revenue produces. The Postal Service should rebalance the cost coverage and unit contributions among First-Class Mail products by lowering prices on more profitable and price sensitive Presort letters. *See* Econometric Demand Equation Tables for Market Dominant Products as of January 2014 (Filed Jan. 20, 2015).

Rebalancing the unit contribution among products within First-Class Mail Letters to preserve and encourage the growth of its most profitable products would improve the Postal Service's financial position and create a more equitable price schedule.

¹ *See* USPS-FY14-1, Public_FY14CRA, "Cost1"; FY2013 ACR at 10, Table 1: First-Class Mail Volume, Revenue, and Cost by Product; FY2012 ACR at 8, Table 1: First-Class Mail Volume, Revenue, and Cost by Product; FY2011 ACR at 16, Table 1: First-Class Mail Volume, Revenue, and Cost by Product; FY2010 ACR at 18, Table 1: First-Class Mail Volume, Revenue, and Cost by Product; FY2009 ACR at 22, Table 1: First-Class Mail Volume, Revenue, and Cost by Product; FY2008 ACR at 18, Table 1: First-Class Mail Volume, Revenue, and Cost by Product.

B. First-Class Mail and Standard Mail Automation Letter Rate Designs Send Inefficient Pricing Signals

The FY2014 ACR shows a passthrough (145 percent) for the First-Class Mail AADC Letters discount that is substantially above 100 percent, *see* USPS-FY14-3, FY14.3 Worksharing Discount Tables.xls, “FCM Bulk Letters, Cards,” while the discount for First-Class Mail 5-Digit Automation Letters passes through only 80.6 percent of the costs avoided. *See id.* The current Standard Mail Automation Letters rate design follows suit - the AADC and 5-Digit passthroughs are 137.5 percent and 81.8 percent, respectively. *See* USPS-FY14-3, FY14.3 Worksharing Discount Tables.xls, “Standard Mail Letters.”

The notice of rate adjustment filed by the Postal Service on January 15, 2015, fails to fully correct these inefficient price signals. *See* United States Postal Service Notice of Market Dominant Price Adjustment (Jan. 15, 2015) (“Notice”). The proposed rate adjustment sets the passthrough for the First-Class Mail AADC Letters discount at 100 percent of the costs avoided, but the First-Class Mail 5-Digit Automation Letters passthrough, at 74.2 percent, moves even farther away from full recognition of the costs avoided by the Postal Service. *See* Notice, Attachment B.xls (“Attachment B”), “FCM Bulk Letters, Cards.” The Standard Mail rate design is essentially unchanged - the AADC and 5-Digit passthroughs are 131.3 percent and 86.4 percent, respectively. *See id.*, Attachment B, “Standard Mail Letters.”

The Postal Service ought to set workshare passthroughs as close as practicable to 100 percent of the costs avoided. Doing so would promote efficiency, lower the total combined costs for mailers, and encourage the retention and growth of its most finely-presorted and profitable products. Because the Postal Service is the only buyer for upstream services in connection with market dominant products there is a temptation for the Postal Service to reduce worksharing

discounts below avoided costs.² Setting workshare discounts at less than costs avoided is exclusionary; the Commission should not allow the Postal Service to price below cost.³

C. FY2014 ACR Data Suggest the New Meter Rate is Having a Positive Effect on Mail Use by Small and Medium-Sized Business Mailers

The new metered letter rate category serves a number of important functions. It serves as the single-piece benchmark for calculating First-Class Mail Automation Letter prices. It helps the Postal Service segment its retail and commercial single-piece customers in a revenue-neutral way by deaveraging single-piece prices. It provides an incentive for small and medium-sized business mailers to stay in the mail and to use the mail in new ways to grow their businesses. It also benefits the Postal Service by encouraging more single-piece mailers to use a more efficient, secure payment channel; thus helping the Postal Service avoid the operational and transaction costs associated with retail stamp sales.

The FY2014 ACR data suggest that the Metered Letters rate is having a positive effect on mail use by small and medium-sized business mailers. The Metered Letters rate was in effect for two full quarters in FY2014. During that period, billing determinants show that the metered mail component of single-piece, nonresidual letters increased from 37.8 percent to 42.4 percent. Calculated from USPS-FY14-4, FY 2014 FCM.xlsx, “A-1 Single-Piece Letters,” cells F12:G13. The billing determinants also suggest that the increase in metered mail letters was due primarily to a decline in non-metered single-piece letters. *See id.*

The FY2014 ACR data are consistent with the experience of international posts that have introduced channel-based pricing to incentivize metered mail. For example, anecdotal feedback

² See Dkt. No. ACR2011, Comments of John C. Panzar on behalf of Pitney Bowes Inc. (ACR2011 Panzar)(Feb. 3, 2012) at 13.

³ See ACR2011 Panzar at 5 (“Reducing discounts below Postal Service avoided costs for any reason is a form of exclusionary pricing. This vertical price squeeze would exclude more efficient competitors from performing upstream services. This would have a short-term negative effect on the productive efficiency.”)

from meter customers in Canada show that small and medium-sized businesses increase their meter through-put or slow the rate of their mail volume decline in response to pricing incentives for metered mail.

The FY 2014 ACR data are limited, but the increase in the metered mail volume suggests that a meaningful price differential between the metered letters rate and the single-piece stamped letters rate is beneficial and should be continued and increased.

D. First-Class Flats Costs

Pitney Bowes explained in Docket No. RM2011-3 that the Postal Service's Cost and Revenue Analysis appears to overstate the cost of First-Class Mail Presort Flats, thereby understating the cost difference between Single-Piece and Presort Flats. *See* Dkt. No. RM2011-3, Comments of Pitney Bowes Inc. (Feb. 18, 2011) at 2-3. Pitney Bowes again urges the Postal Service to improve the First-Class Mail Presort Flats costing methodology for future Annual Compliance Reports.

III. CONCLUSION

Pitney Bowes appreciates the Commission's consideration of these comments.

Respectfully submitted:

/s/

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